WYOMING LEGISLATIVE SERVICE OFFICE

Memorandum

DATE	July 9, 2018
TO	Task Force on UW Housing
FROM	Subcommittee on Financing Options
SUBJECT	Initial Report on Financing Options for UW Housing

The UW Housing Task Force's Subcommittee on Financing Options met by person in Cheyenne and via teleconference on June 28th to discuss and explore various options that may be available to UW to fund a proposed student housing project. Attending the meeting were Chairman Harshman, Rep. Bob Nicholas, UW Trustee John McKinley, State CIO Patrick Fleming, UW VP for Student Affairs Sean Blackburn, and UW Director of Residence Life and Dining Eric Webb, and LSO staff Dawn Williams and Matt Obrecht. Handouts were provided by Mr. Fleming, Mr. Blackburn and Mr. Webb, and by LSO (attached and incorporated herein where relevant).

The Subcommittee determined that while there are benefits and drawbacks of funding from the State or through a Public-Private Partnership (P3), State funding is likely the better option for the project.

Costs of the Housing Project

The Subcommittee discussed what level of funding would be needed. The consensus is that construction cost per bed is likely to be around $100,000. Depending on the number of beds constructed, the costs of infrastructure, demolition of existing facilities, etc. are likely $50,000,000 to $100,000,000. If the retirement of existing UW bonds is included in the financing calculation ($87,000,000), the likely cost for 1000 new beds is approximately $250,000,000 to $300,000,000 and the cost for 2000 new beds is $350,000,000 to $400,000,000.

Patrick Fleming and Amy Aponte of Balfour Beatty both provided budget/funding scenarios of student housing for consideration of the task force in separate documents.

Case Studies of LSU and CSU

The Subcommittee also asked for information on why Louisiana State University chose a P3 structure for their recent housing expansion and why Colorado State University instead chose state issued bonds for its funding. Patrick Fleming reached out to Patrick H. Martin, Assistant Vice President Real Estate, Public Partnerships, and Compliance at LSU for his perspective. Following is an excerpt from Mr. Martin's response:

> The speed for us was huge. Cutting 2 years off of planning/approval time means 2 years less of construction cost inflation and interest rate risk. We also got a better rate for architects, 4% versus the Louisiana state standard for government jobs of 7%. Some of that is offset by the developer payment, which for us was a total of 4%. Our planning, design, and construction staff also have found very positive results by using a design-build method of contracting, where you hire the contractor as a Construction Manager at Risk… the general contractor essentially bids for the job on what percentage he will charge as a management fee, and then bids out all the subcontractor work. The CMAR gets his percentage of the sum of the subcontractor bids. Here in Louisiana, we can't really do design-build in the state contract realm, but we could in the P3 world. With design-build, you get the contractor and the architect sitting together at the design table, which we found generated some cost savings, but also substantially increased our speed to construction.
>
> The other key is long-term operations. The true idea of the P3 is that you transfer the costs and risks of long-term maintenance to the developer. That is not feasible in the traditional state construction contract process. You want the private partner to make the decisions that lead to the lowest total cost of ownership over the life of the buildings. Personally, I find that the university still needs to pay close attention to those trade offs, and if you're not careful, you end up with a developer that will soak you over time. But not always, and you can get real benefit here with (again) proper planning.
>
> In general, you are absolutely correct that looking purely at construction costs, you won't get real savings from the P3 model. The savings come in from design efficiencies, cutting time off the project, and transferring some risks to the developer, both up front and long-term.

Matt Obrecht and Dawn Williams spoke with Mari Strombom, Executive Director of Housing and Dining Services at CSU concerning the university's decision to issue bonds rather than build with a P3. Ms. Strombom stated that CSU never considered a P3 option because it had the support of the administration to bond student housing projects. Ms. Strombom further related that in speaking with colleagues at other institutions around the country, it appeared that P3 was utilized only when other funding was not available. Furthermore, state funding was the more attractive option for CSU because the university could have more control over the project. Ms. Strombom stressed the importance of designing a project for student success as the primary goal rather than profit motivation. This allowed CSU to focus more on co-learning centers within student housing and other public areas like group kitchens, over an attempt to maximize the number of beds. She also stated the importance to CSU of staffing and maintaining the buildings with university personnel to ensure that they are maintained to CSU's standards. Ms. Strombom related an experience at Northern Arizona University where it was assumed that student housing located on the main campus area, which was managed by the P3 developer, was a university managed property. Complaints about the property were directed to the university, only to be redirected to the P3 operator. This lead to confusion and frustration.

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Pros and Cons of P3 v. State Funding

The Subcommittee developed a list of pros and cons of utilizing some form of P3 structure for the UW Housing Project.

Pros:

1. P3 is an attractive option to fund a project when the institution does not have readily available cash or borrowing capacity.
2. The structure of a P3 is flexible in many ways to provide the institution with varying levels of involvement to suit its needs.
3. The developer of a P3 project is likely to have expertise in the field and a long and successful track record of developing and managing these types of projects around the country. The UW Housing Project could benefit from this expertise.
4. Utilizing a P3 structure to build student housing would allow for available cash or bonding capacity to be used for other projects that don't have a revenue source.
5. P3 can finalize a project quickly, potentially in much less time than a State/UW managed project.

Cons:

1. With a P3 there is likely a greater cost than with issuing bonds or utilizing some form of a loan from the State. Bonds currently carry an interest rate of between 3% to 3.5% and most P3 projects have an additional 5% financing cost in consideration of the additional risk the private developer is assuming.
2. Utilizing the P3 structure would create a profit center for a private company on the core grounds of the only university in the state. This would put many local residential developers and managers at a substantial disadvantage.
3. With a P3 contract, because it is not technically a "state" project for the purposes of the Wyoming procurement statutes, there is no requirement for Wyoming contractors, subcontractors, or materials to be used on the project.
4. A P3 project could result in less involvement in key decision making by UW Trustees, the Legislature, and Laramie/Wyoming residents.
5. Currently, at the one existing P3 on the UW campus, rental revenues do not cover annual costs, which results in UW having to annually supplement payments to the P3 developer with other sources of funds. There is a potential for this to happen with the new UW housing project.
6. There is the potential that the developer of the P3 could sell the project to another operator, which would require UW to work with a new operator that may not deliver the same level of service as the original developer.
7. A P3 project could negatively impact current employees of UW who would lose their jobs and may or may not be offered private positions, likely at different terms of employment.
8. With a P3 project, because there is a profit motive, the quality of the construction and maintenance of the facility may not be at the same level as a UW constructed and managed facility.

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9. Financing a P3 requires a higher debt service ratio than is required for general obligation bonds or revenue bonds.

State Funding Options

If State funding is utilized for the project, there are likely a multitude of paramutations, procedures, terms and conditions available for the State to fund the UW housing project, but all of those options really boil down to three core principles: 1) Direct appropriation; 2) Bonding; or 3) a Public Purpose Investment. Of course, the Task Force could recommend, and the Legislature could decide, to adopt a combination of these options, as well. These three options are presented below.

(A). Direct Appropriation:

On its face this is the most straightforward funding option, but there are still significant variables available to the Legislature when exercising this option. The Legislature could appropriate all of the needed project funding at one time, likely from the Legislative Stabilization Reserve Account (LSRA), with no requirement for a payback. The Legislature could dedicate funding from a revenue stream or streams, to an account created for the specific purpose of funding the UW Housing Project. Potential available sources of revenue include federal mineral royalties (FMRs), the statutory 1% severance tax (approximately $90 to $100 million a year as of FY 2018), or the earnings from the Permanent Wyoming Mineral Trust Fund (PWMTF), which are directed to either the LSRA or the Strategic Investment and Projects Account (SIPA) (roughly $87 million right now is directed to both accounts if earnings on the PWMTF reach or exceed the spending policy). Depending on the magnitude and proportion of each dedication, it could take multiple biennia to reach the total funding level. Another option with a direct appropriation (or really any funding option) would include creating "phases" of the project. The phases of construction could be spread over several years, with funding from revenue streams becoming available when each "phase" is ready for construction to commence or contracts to be let.

Another direct appropriation option is to provide UW a loan for the housing project. Such a loan would not have the same potential constitutional implications of a Public Purpose Investment (PPI) from the PWMTF, and a lower interest rate may be available, potentially as low as 0%. The legislation could also dedicate a stream of revenue for repayment of the loan, just like a PPI, such as UW's FMR stream or the student lease revenue from the new residence halls.

(B). Bonding:

There are two forms of bonds available for this project: general obligation or revenue bonds. General obligation bonds are paid by pledging future tax revenues. Revenue bonds are paid by pledging future non-tax revenues. Each type of bond has its own legal requirements and limitations.

General obligation bonds create debt in the constitutional use of that term because there is the present legal potential that the issuing governmental entity will have to exercise its power to tax to pay such bonds. Thus, the issuance of state general obligation bonds triggers the State's debt limit under Article 16, Section 1 of the Wyoming Constitution, which prohibits the State from creating debt more than 1% of the total statewide assessed property valuation as shown by the last general assessment. The last certified total statewide assessed valuation was $18,825,099,205. The current 1% general obligation limit, then, is $188,250,992.05. The issuance of state general obligation bonds also triggers the election requirement in Article 16, Section 2.

Revenue bonds entail payment pledges that do not create debt in the constitutional use of that term because there is no present legal potential that the issuing governmental entity will have to exercise its power to tax to pay such bonds. Revenue bondholders can seek repayment only from pledged revenue sources. The issuance of state revenue bonds, therefore, does not trigger the debt limitation under Article 16, Section 1 or the election requirement in Section 2. Non-tax state revenue sources that are available to pledge include federal mineral royalties and coal lease bonus payments, as well as earnings from investments, e.g., a pledge of general fund revenues from the Permanent Wyoming Mineral Trust Fund or a pledge of earnings from the corpus of other permanent land fund accounts, if the earnings are not constitutionally dedicated to another use.

As outlined by Patrick Fleming in his report to the Task Force on June 19, tax-exempt municipal bonds are trading at rates less than US Treasuries if the issuer has a AA+ rating or better. Bonding the amount of funds needed for the UW Housing Project would require a substantial dedication of revenue streams from UW and the State to receive the necessary credit rating. It's also not clear whether the UW Supplemental Coverage Program would yield any appreciable benefits in this scenario given the magnitude of the funding under consideration.

(C). Public-Purpose Investment:

This option would require legislation to authorize a public purpose investment (PPI) from the PWMTF. Public purpose investments are those authorized or directed by state law for investment of state funds for purposes other than for pure investment return purposes. That is, the investment has some additional indirect public purpose. There are examples of PPIs that would fall in the same category of UW housing bonds as precedent: industrial development bonds, mortgage backed securities, time-deposit open accounts (benefiting Wyoming banks) and farm loans. A PPI from the PWMTF is different than a loan to a public subdivision from the PWMTF in that there likely has to be some form of financial return to the State on its investment in a PPI. How that return is realized is open for discussion.

By statute the Legislature has stated that the Uniform Prudent Investor Act shall govern state investments. (W.S. 9-4-715(d)(i)) Within that Act, W.S. 4-10-911 provides: "This article applies to public funds of the state of Wyoming unless a different investment standard is specifically provided for the investment of specified public funds." Generally, in accord with the Prudent Investor Act is the common law duty of the Treasurer - as a fiduciary to exercise diligent and prudent care over public funds under his purview. (See, Wyo. Att. Gen'l op. 77-19, citing State v. Gramm, 52 P. 533 (Wyo. 1898)).

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Public purpose investments have carried interest rate ranges from 0% (until the project was built) to over 8%. The lowest overall rate from the PWMTF was 1.5% for the Laramie Territorial Park (which started at 6%). While by no means making all public purpose return rates uniform, the Legislature in the past ten years or so has often used a more uniform standard, tied in some manner to the rate of return foregone by not investing solely in accordance with the state investment policy. The Legislature could determine that the return on investing in university housing can outweigh the return on investments in securities or other investments which might appear greater on their face. This general proposition, that the immediately identifiable return need not be the sole consideration in managing trust funds, finds support in Wyoming caselaw concerning school trust lands. Frolander v. Ilsley, 264 P.2d 790 (Wyo. 1953).

In this instance, similar to a loan, the Legislature could dedicate a stream of revenue for repayment of the PPI to the PWMTF, such as UW's FMR stream or the student leases.

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